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No. 86-61

In the Supreme Court of the United States

OCTOBER TERM, 1986

COMMONWEALTH ELECTRIC COMPANY, PETITIONER

v.

DEPARTMENT OF PUBLIC UTILITIES OF THE COMMONWEALTH OF MASSACHUSETTS

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME JUDICIAL COURT OF MASSACHUSETTS

BRIEF FOR THE UNITED STATES AND THE FEDERAL ENERGY REGULATORY COMMISSION AS AMICI CURIAE

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QUESTION PRESENTED

Whether, under the circumstances of this case, the Federal Power Act, 16 U.S.C. 824 *et seq.*, barred the Massachusetts Department of Public Utilities from (a) attributing to a retail seller of electric power a portion of the "imprudence" of its wholesaler in managing a nuclear power plant and therefore (b) denying the retailer's request to recover in its retail rates certain power purchase costs due to an outage at the nuclear plant.

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This brief is filed in response to the Court's invitation to the Solicitor General to file a brief expressing the views of the United States.

STATEMENT

1. The Federal Power Act, 16 U.S.C. 824 *et seq.*, gives the Federal Energy Regulatory Commission exclusive regulatory authority over "the regulation of interstate wholesale utility rates" (*Nantahala Power*

& Light Co. v. *Thornburg*, No. 85-568 (June 17, 1986), slip op. 12). Rates for the sale of power at retail are regulated by the states, but "a state utility commission setting retail prices must allow, as reasonable operating expenses, costs incurred as a result of paying a FERC-determined wholesale price" (*id.* at 11). That is, under the "filed rate doctrine" and the "*Narragansett* doctrine," in order to avoid a prohibited " 'trapping' of costs" (*id.* at 17), the FERC-filed wholesale rate paid by a utility must be treated as "reasonable" by the state regulatory commission in setting retail rates.[1] However, this Court has not resolved the extent to which a state commission may determine for itself, in a retail proceeding, "the reasonableness of purchasing power from a particular source of, rather than paying a particular rate for, FERC-approved power" (*id.* at 18-19).

2. Boston Edison Company is the operator of the Pilgrim I nuclear plant; it also sells electric power at both wholesale and retail to Massachusetts customers. Commonwealth Electric Company, the peti-

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[1] The Federal Power Act requires that utilities file with the Commission "schedules showing all rates and charges for any * * * sale subject to the jurisdiction of the Commission, and the * * * contracts which in any manner affect or relate to such rates * * *." 16 U.S.C. 824d(c). Under the filed rate doctrine, established in *Montana-Dakota Utilities Co.* v. *Northwestern Public Service Co.*, 341 U.S. 246, 251-252 (1951), "the right to a reasonable rate is the right to the rate which the Commission files or fixes, and * * * the courts can assume no right to a different one * * * ." Under the *Narragansett* doctrine articulated in *Narragansett Electric Co.* v. *Burke*, 119 R.I. 559, 381 A.2d 1358 (1977), cert. denied, 435 U.S. 972 (1978) and endorsed by this Court in *Nantahala*, a state utility agency is required to treat such a FERC-filed rate as "reasonable" (see 119 R.I. at 566, 381 A.2d at 1362).

tioner here, is a public utility that purchases electric power at wholesale and sells electric power at retail to Massachusetts customers. In August 1972, Boston Edison and petitioner agreed that for 28 years petitioner would purchase 11% of the power from Boston Edison's Pilgrim I nuclear plant (see Pet. App. 76a-117a). As the Federal Power Act requires (see note 1, *supra*), petitioner and Boston Edison filed the contract with the Commission, which allowed it to become effective.[2]

From December 7, 1981 to April 8, 1982, the Pilgrim I plant was shut down. During that outage both Boston Edison and petitioner purchased replacement power (under other FERC-filed contracts) that was more expensive than the power they had been receiving from Pilgrim I. When Boston Edison applied to the Massachusetts Department of Public Utilities (DPU), the state regulatory agency, for a retail rate increase to recover the additional cost of that replacement power, the DPU ruled that the Pilgrim I outage was caused by Boston Edison's imprudent plant management (see Pet. App. 39a). When petitioner later applied to the DPU for a similar increase, the DPU denied petitioner's application (*id.* at 28a-30a, 39a-44a), noting that it had previously denied Boston Edison's application (*id.* at 29a, 39a). In petitioner's proceeding, the DPU determined that, under the contract between the two utilities, peti-

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[2] The Commission followed its customary practice of issuing notice of the proposed filing. No comments were received, and the Commission accepted the contract for filing and ruled that it should become effective as of December 9, 1972. The Commission did not purport to interpret the contract or any of its clauses, and it notified the parties that the acceptance for filing did not constitute approval of the contract terms. See Pet. App. 118a-119a.

tioner "shares responsibility for [Boston Edison's] imprudence during the Pilgrim I outage" (*id.* at 41a). The DPU focused on a contractual provision specifying that Boston Edison did " 'not guarantee a constant supply of * * * electricity' " and that petitioner " 'assume[d] the risks on non-delivery of electricity * * * to the same extent as if it were itself operating [Pilgrim I] for the purpose of supplying itself with electricity' " (*ibid.* (quoting Section A-3.1 of the contract)).

The DPU rejected the claim that a different provision in the contract (Section 2.3) set forth petitioner's obligations to its retail customers in the event of an outage. Section 2.3 of the contract states that if, as a result of an outage, "no deliveries are made * * * for one or more periods of at least one hundred twenty (120) consecutive days each, the term of this Agreement * * * will be extended for a period equal to the aggregate of such periods" (Pet. App. 82a). In the DPU's view, while "[s]uch a clause could possibly mitigate damages" in other circumstances, "this particular contract extension, almost twenty years in the future," was insufficient to mitigate damages in this case since "[t]he present value of the benefit is tremendously speculative" (*id.* at 42a). Rather than rely on such uncertain future events, the DPU gave petitioner's retail ratepayers immediate rate relief; the agency reduced petitioner's proposed rate increase by the incremental amount the utility paid for replacement power during the outage, $552,513 (*id.* at 44a).

3. On appeal, the Supreme Judicial Court of Massachusetts affirmed the DPU order (Pet. App. 1a-26a). The court relied on the contractual provisions (*id.* at 6a-7a & n.1) and the state law "schem[illegible]f

public utility regulation" (*id.* at 8a) to hold that "[t]he DPU was warranted in finding that the provisions of the contract reveal the company's intent to be treated as a joint owner and impose the kinds of risks and obligations ordinarily associated with ownership" (*id.* at 8a-9a).

The court next rejected petitioner's claim that federal law preempted the challenged state regulatory action. The court reached that conclusion by applying the standards for assessing claims of preemption established by this Court. First, the court stated that in enacting the Federal Power Act Congress did not "occupy the field of regulation of electricity sales * * * [but] left regulation of sales at retail to the States" (Pet. App. 17a). Next, the court found that petitioner had failed to show that the DPU decision was in " 'actual conflict' " with any federal regulation or that there was a "physical impossibility of compliance with both State and Federal direction" (*ibid.* (quoting *Florida Lime & Avocado Growers, Inc.* v. *Paul*, 373 U.S. 132, 142-143 (1963)). Finally, the court considered whether the DPU decision posed an obstacle to realizing the purposes and objectives of the Federal Power Act. Finding no such obstacle, the court held that since this case involves retail ratemaking the state's "inquiry into the prudence of a retail seller in choosing the source of its supply and in incurring particular costs" did not disturb the federal regulation of rates for wholesale transactions (Pet. App. 19a).

The court ruled also that the DPU's decision did not constitute a collateral attack on FERC's approval of the Boston Edison-Commonwealth contract: "[b]ecause FERC does not have jurisdiction over retail rates, the issue raised here could not, and

should not, have been raised [in the federal administrative process]" (Pet. App. 20a-21a).[3]

DISCUSSION

Although the opinions of the Massachusetts DPU and the Supreme Judicial Court do not make the basis for the state determination entirely clear, we think they are best read to base the denial of the rate increase requested by petitioner on narrow grounds that do not present any question of general importance under this Court's decision in *Nantahala* or under the filed rate and *Narragansett* doctrines. Accordingly, we believe that the case does not warrant this Court's review.

1. In *Nantahala*, this Court reserved the question whether "a particular *quantity* of power procured by a utility from a particular source could be deemed unreasonably excessive if lower-cost power is available elsewhere, even though the higher-cost power actually purchased is obtained at a FERC-approved, and therefore reasonable, *price*" (slip op. 19 (emphasis in original)). Both the state court (Pet. App. 19a-20a) and the parties (Pet. 15-16; Br. in Opp. 11-18) suggest that this case presents a version of that question. We disagree: the DPU did indeed bar petitioner from recovering its costs of purchased power on the ground that the purchases were necessitated by imprudence; but the imprudence here—

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[3] One judge dissented (Pet. App. 23a-26a). He would have remanded for the DPU to decide whether FERC had "determined that the agreement was just and reasonable from the point of view of Commonwealth" (*id.* at 25a). If the state agency found that FERC had made such a determination, then the dissenting judge would have concluded that the DPU interpretation of the contract was preempted.

plant mismanagement partially attributed to petitioner by virtue of its contract with the plant operator—is of a different sort from that hypothesized in *Nantahala* and does not, under the circumstances, present questions of general significance.

The denial of the rate increase sought by petitioner was based on two determinations by the Massachusetts DPU, each of which it was entitled to make only because of the somewhat unusual circumstances of this case. First, the DPU determined that Boston Edison, the operator of Pilgrim I, had mismanaged the facility and was responsible for the outage; the DPU had occasion, and jurisdiction, to make such a determination with respect to petitioner's vendor because of the coincidence that Boston Edison also sells power at retail and had applied for, and been denied, a rate increase. Second, the DPU determined that the particular terms of the FERC-filed contract between Boston Edison and petitioner made petitioner responsible for a share of the consequences of the mismanagement of Pilgrim I; the DPU had jurisdiction to make this determination only because FERC had not had occasion to interpret the contract in this respect.[4]

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[4] We fully agree with petitioner (Pet. 14) that a state may not "avoid the 'bright line' between federal and state jurisdiction and the statutory procedure for FERC review of wholesale performance * * * by discovering imprudence in the chain of electric supply and then imputing such imprudence to the retail electric company over which it has jurisdiction * * *." But that is not what happened here: the DPU found imprudence in a retail rate proceeding involving a utility (Boston Edison) over which it had jurisdiction and which it found to have acted imprudently; it imputed the imprudence in respect of the same outage to petitioner because it found warrant for doing so in a contract that had not yet been inter-

Neither determination presents an issue of general importance under *Nantahala*. First, plant mismanagement is quite different from the imprudence under discussion in *Nantahala*. The allegation that a utility selling at retail should have chosen to acquire power from Source A, rather than from Source B under a FERC-filed rate schedule, may raise a significant question as to whether the state regulator has power to resolve that issue (see *Nantahala*, slip op. 19, citing *Pike County Light & Power Co.* v. *Pennsylvania Public Utility Comm'n*, 77 Pa. Commw. 268, 273-274, 465 A.2d 735, 737-738 (1983)). But the allegation that a utility selling at retail is not entitled to recover the cost of purchased power because it has mismanaged its production facility raises no such question: it is clear that the state regulator may deny a rate increase on that ground, as the Massachusetts DPU did with respect to Boston Edison. See *Violet* v. *FERC*, 800 F.2d 280, 282 (1st Cir. 1986) (citing *Missouri ex rel. Southwestern Bell Telephone Co.* v. *Public Service Comm'n*, 262 U.S. 276, 289 (1923) (Brandeis, J., concurring)).[5]

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preted by FERC. Had Boston Edison sold power only at wholesale, its right to pass on to its customers its costs resulting from the outage, and its obligation if any to reimburse customers for costs incurred by them, could only have been determined by FERC, which would have had to resolve any question of plant mismanagement or of contract interpretation necessary to determine Boston Edison's rights and obligations. Conversely, had petitioner been the manager of its own power production facility, there would be no question of the state's power to deny a retail rate increase on the basis of a state finding that the facility was mismanaged. See, *e.g.*, *Violet* v. *FERC*, 800 F.2d 280, 282 (1st Cir. 1986).

[5] Petitioner contends (Pet. 19) that it was not afforded an opportunity to rebut the charge of mismanagement by Boston

The DPU's second determination—that petitioner could be held partially responsible for the imprudent management of Pilgrim I—presents a more difficult question. But although there is language in both the DPU and state court opinions that we find troubling,[6] we agree with the court that, at bottom, the DPU decided that question "based on the provisions of the contract between [petitioner] and Boston Edison" (Pet. App. 5a). Under the circumstances of this case, neither the assumption by the Massachusetts DPU of the burden of interpreting the contract, nor the interpretation it reached, presents any question of wider importance.

A FERC interpretation of the contract would of course have been binding on the parties and the

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Edison. Respondent disputes this as a factual matter (Br. in Opp. 26). In any event it does not present an issue that warrants this Court's consideration.

[6] For example, the court stated (Pet. App. 7a n.2) that "actual or constructive ownership is [not] a prerequisite to imputation of imprudence to a public utility. * * * It is not the company's similarity to an owner that is dispositive, however, but its nondelegable statutory obligations."

If the court was suggesting that, notwithstanding the terms of a FERC-filed contract, a utility selling at retail may have a duty under state law to obtain better terms or performance from its wholesaler than the contract prescribes, or that it may bear automatic (rather than contractual) responsibility for its wholesaler's performance, the suggestion is entirely incorrect. Any such "nondelegable duty" (see also *id.* at 9a n.4) would impeach the FERC-filed contract in a manner clearly barred by *Nantahala*. In this case, however, we read the court's decision as resting on an interpretation of the contract that imposes actual or constructive ownership obligations on petitioner; the suggestion that such a finding would not have been necessary is erroneous but appears to be dictum. See Pet. App. 7a & n.2.

DPU. FERC is responsible for ensuring that all rates or charges made, demanded, or received by any public utility for or in connection with the transmission or sale of electric energy in interstate commerce are "just and reasonable" (16 U.S.C. 824d(a)). The Commission therefore exercises exclusive authority to set rates and to approve or modify contracts at the wholesale level. See, *e.g.*, *Nantahala*, slip op. 10 (quoting *Arkansas Louisiana Gas Co.* v. *Hall*, 453 U.S. 571, 581 (1981). And where FERC has interpreted a filed contract, its interpretation becomes part of the filed rate, and ~~that~~ the state is bound to honor it. See *AEP Generating Co.*, 38 Fed. Energy Reg. Comm'n Rep. (CCH) ¶ 61,243, at 61,823 (1987); *AEP Generating Co.*, 32 Fed. Energy Reg. Comm'n Rep. (CCH) ¶ 61,364, at 61,821 (1985), on reh'g, 36 Fed. Energy Reg. Comm'n Rep. (CCH) ¶ 61,226, at 61,549-61,550 (1986).[7] But where the Commission has not provided an interpretation, the state may do so when necessary to fulfill its obligation to set retail rates. *Ibid.*[8]

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[7] Petitioner could have sought an interpretation of its contract from FERC prior to the DPU and state court proceedings and, indeed, may still do so now. See, *e.g.*, *AEP Generating Co.*, on reh'g, 36 Fed. Energy Reg. Comm'n Rep. (CCH) ¶ 61,226, at 61,551 n.3 ("there are, and have been, a variety of procedural options available for a party to solicit such an interpretation. For example, the utilities or any affected state commission could have requested a declaratory order [from FERC] as soon as a disagreement became evident."); *Kentucky Power Co.*, 36 Fed. Energy Reg. Comm'n Rep. (CCH) ¶ 61,227, at 61, 554 (1986).

[8] Should the Commission later interpret a contractual provision previously interpreted by the state, the federal interpretation would preempt any conflicting state interpretation (even though the state's view would have been acceptable and

A state interpretation that effectively modifies the terms of the FERC-filed contract would of course be preempted by the federal regulatory scheme.[9] And it may be difficult in some cases to draw the line between permissible contract interpretation and impermissible contract modification. In the present case, the DPU found that petitioner had, by contract "assumed the risks of ownership" (Pet. App. 40a), that "in this instance [petitioner's] life-of-the-unit contract creates [in petitioner] the obligations and privileges of a joint owner" (Pet. App. 41a), and that accordingly petitioner "shares responsibility for [Boston Edison's] imprudence" (*ibid.*). The state court affirmed this reading. While that is not necessarily the reading FERC would have endorsed had it been presented with this question of contract interpretation, we cannot conclude that the result was impermissible (in the absence of a FERC determination to the contrary) or that it presents any question that merits this Court's review.[10]

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controlling in the absence of Commission action). See *AEP Generating Co.*, 38 Fed. Energy Reg. Comm'n Rep. (CCH) ¶ 61,243, at 61,823 (1987).

[9] In some circumstances, not present here, the Commission effectively has exclusive jurisdiction over the interpretation of contracts. For example, a state would have no role in regulating a contract for wholesale transactions between the subsidiaries of a fully integrated holding company. See *AEP Generating Co.*, 38 Fed. Energy Reg. Comm'n Rep. (CCH) ¶ 61,243; *Mississippi Industries* v. *FERC*, 808 F.2d 1525, 1547-1549 (D.C. Cir. 1987), petitions for cert. pending, No. 86-1380 (filed Feb. 20, 1987), No. 86-1424 (filed Mar. 4, 1987), reh'g en banc granted on other grounds, No. 85-1611 (D.C. Cir. Apr. 3, 1987).

[10] The state court's rejection of Commonwealth's argument concerning the outage provision (Section 2.3) may also be

2. This case does not present any issue of general significance under the filed rate and *Narragansett* doctrines. As described above, it arose in an atypical fact situation—the happenstance that the same state regulator had jurisdiction, and the opportunity, to determine, in different retail rate proceedings, both the question of the mismanagement of the plant by one utility and the question of imputation of that mismanagement to another utility. Moreover, the case turns on the ultimately factual determination of mismanagement and on the interpretation of a contract that FERC had not had occasion to interpret. The case therefore does not warrant an exercise of this Court's certiorari jurisdiction.

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justified as permissible contract interpretation. Section 2.3 may be read to govern only the relationship between the two utilities, thus creating a remedy that Commonwealth could invoke against Boston Edison but not altering the fact that under the contract Boston Edison and petitioner shared responsibility for the outage. While neither the state court nor the DPU expressly relied on that interpretation of Section 2.3, they reached the same result that that interpretation would have produced.

Both the DPU (Pet. App. 42a n.1) and the state court (*id.* at 8a-10a) found as a matter of public policy that Commonwealth could not insulate imprudent plant management from review in retail ratemaking proceedings. We do not agree that that proposition would govern in every case. For example, if FERC approved a contract or rate schedule that precluded review of particular subjects in retail ratemaking proceedings, then state scrutiny of those subjects would be barred. The question raised by this hypothetical is not, however, present in this case.

Finally, this case is not like *Arkansas Louisiana Gas Co.* v. *Hall*, 453 U.S. at 578-579, in which the state court ordered a remedy—an actual change in the wholesale rate—that directly and clearly conflicted with the rate on file with FERC.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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